

VZCZCXRO0736

RR RUEHAG RUEHDF RUEHIK RUEHLZ RUEHROV
DE RUEHCV #0358/01 0472128

ZNR UUUUU ZZH

R 162128Z FEB 07

FM AMEMBASSY CARACAS

TO RUEHC/SECSTATE WASHDC 7887

INFO RUCNMEM/EU MEMBER STATES COLLECTIVE

RUEHWH/WESTERN HEMISPHERIC AFFAIRS DIPL POSTS

RHEHNSC/NSC WASHDC

RHEBAAA/DEPT OF ENERGY

RUCPDOC/DEPT OF COMMERCE

UNCLAS SECTION 01 OF 02 CARACAS 000358

SIPDIS

SENSITIVE

SIPDIS

TREASURY FOR KLINGENSMITH AND NGRANT
COMMERCE FOR 4431/MAC/WH/MCAMERON
NSC FOR DTOMLINSON
ENERGY FOR CDAY, DPUMPHERY, AND ALOCKWOOD

E.O. 12958: N/A

TAGS: ECON ENRG PGOV VE

SUBJECT: CHAVEZ TO LOWER VAT, "STRENGTHEN" CURRENCY AND
PUNISH HOARDERS

CARACAS 00000358 001.2 OF 002

11. (SBU) Summary: On February 15, Chavez announced a two stage reduction of the value added sales tax (VAT), which will reduce the tax from 14 percent to 9 percent by July 12007. He also presented a plan for "monetary reform," removing three zeroes places from the bolivar by 2008, to create the appearance of a strong currency. Chavez announced that he would sign a decree-law on February 16 giving him to power to nationalize supermarkets and food distributors and criminalize speculation and hoarding. End Summary.

Lowering the IVA by 5 Percentage Points

12. (SBU) During his newly-formulated call-in television program "Alo Presidente" on February 15, Chavez announced that the VAT would be reduced from 14 percent to 9 percent in a two phase process. The first phase will take effect March 1 and reduce the VAT by three percentage points. The second phase will lower the tax two more points by July 1. Chavez explained that the VAT was a regressive tax that burdened low-income Venezuelans. He said that the VAT reduction is part of his anti-inflationary plan and estimated that the 5 point reduction in the VAT would result in a 3 point reduction in inflation. He conceded that this package would cost the BRV approximately USD 3 billion per year in revenue, which he claimed was greater than the budget of the Ministry of Defense. He strongly urged SENIAT to more strictly enforce income tax (ISLR) collection. Chavez said that the revolution would reduce the VAT progressively, and ultimately eliminate it entirely. The BRV would make up lost revenue through measures to target the wealthy, such as property and luxury taxes. "Those who have a lot of wealth need to pay tax," added Chavez.

A Strong Bolivar

13. (SBU) Chavez announced a monetary "reform" (actually a monetary conversion) plan to remove three decimal places from the bolivar, to take effect February 4, 2008. "The bolivar is going to recover all of the land that it lost to the dollar and the euro and all of the monies in the world," proclaimed Chavez. Pointing to 13 trimesters of continued

growth in Venezuela, Chavez said that it was time for Venezuela to have a strong currency that reflected its economic muscle. He explained that the Central Bank was currently reviewing the project and that legal measures and a public information campaign would be underway in the second trimester of 2007.

14. (SBU) Chavez placed the "strong bolivar" in the framework of Venezuela's historic struggle against inflation, arguing that the reform would reduce inflation to one percent. He cited a study, presumably prepared by the Central Bank, that this measure would reduce the average number of bills in the hands of Venezuelans from 30 to 12, simplify transactions for the public, and bring the currency within "international standards." "Monetary reform will permit a more efficient system of payments, consolidate confidence in the national money and produce psychological effects in people's expectations," said Chavez. He packaged the announcement of the strong bolivar in typical rhetoric, saying he was tempted to call the new currency "cachete," historically a strong Venezuelan currency. He noted that the bolivar's decline in value vis-a-vis other currencies began in 1983, the bicentennial anniversary of Bolivar's birth, exclaiming, "the strong bolivar, in honor of Bolivar, in our of our people, in honor and in recognition to the great force that we have come to achieve in these years!"

Law Against Hoarding and Speculation

15. (SBU) Chavez announced that on February 16 he expected to sign, pursuant to the Enabling Law, the final version of "the decree-law of popular defense against hoarding and speculation, boycotts, and any other conduct that affects food whose prices are regulated." This decree-law enables Chavez to initiate expropriation proceedings in all levels of

CARACAS 00000358 002.2 OF 002

the production chain to "protect food security and sovereignty." "From the land where the cattle are, machinery, slaughterhouses and equipment, to the stores. Everything is declared public utility and social interest for this revolutionary law," proclaimed Chavez.

6 (SBU) A visibly emotional Chavez warned, "I implore the cattle owners, producers, meat transporters for example...everything that is regulated...big stores and little ones too, I implore you to not give me reasons. But if you give me them, I am going to expropriate everything that I have to in defense of our people." Chavez responded angrily to comments made by the president of CAVIDEA, Venezuela's Food Industry Council, that if the government did not allow the free sale of meat, it would close the slaughterhouses. "Close the slaughterhouses? I will send the army to take them," Chavez menaced.

17. (SBU) The decree-law enables the BRV to take preventive measures, including occupying facilities, ordering operations to continue that the owners had closed, seizing products, and closures for 90 days with the obligation to pay employee salaries. Penalties include fines and prison terms from 2 to 6 years.

Food into Petroleum

18. (SBU) Continuing on the theme of food security, Chavez announced that he had set aside additional funds for Mercal, the BRV's food distribution network. PDVSA's social fund will provide approximately USD 237 million to Mercal. "Petroleum converted into food, petroleum for the people," said Chavez.

Comment

¶9. (SBU) The return of Alo Presidente showed a Chavez who appeared visibly emotional with respect to "food security," but this is mostly just an act. Chavez understands that his continued support among low-income Venezuelans depends on their ability to buy staple foods at low cost. The cosmetic bolivar conversion may actually raise prices in the short-term as sellers tend to round-up adjusted prices, and is grounded more in Chavez' preoccupation with Venezuela's world image than in economics, where it will have no effect on underlying monetary policy. The proposed 5 point reduction in the VAT means that the BRV will lose approximately USD 3 billion with no clear program of how to make up that lost revenue, worsening the BRV's fiscal predicament. Though couched as an anti-inflationary measure, reducing the VAT would only impact inflation in so far as it would lower prices by sucking out government revenue. With commitments to nationalizations within the past week already over USD 1 billion, Chavez' pronouncements are pure populism under the guise of economic reform. End Comment.

BROWNFIELD